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No. 92-90

In the Supreme Court of the United States

OCTOBER TERM, 1992

VIRTUAL MAINTENANCE, INC., PETITIONER

v.

PRIME COMPUTER, INC., RESPONDENT

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONER

We showed in the petition that the decision below, which was rendered before this Court decided *Eastman Kodak Co.* v. *Image Technical Services, Inc.*, 112 S. Ct. 2072 (1992), conflicts irreconcilably with that decision. Prime describes the relevant facts of *Kodak* in terms that apply equally to this case (Br. in Opp. 6-7). Prime even attached the amicus brief for the United States in *Kodak* to its reply brief in the court below. See Prime C.A. Rep. Br. 13 n.14. Yet Prime now maintains that *Kodak* is irrelevant, in the process accusing Virtual of mischaracterizing the opinion below and the record. Br. in Opp. 10. In fact, it is Prime that has resorted to mischaracterization in an effort to evade *Kodak*'s clear implications.

For example, in the opening paragraph of a key section of its opinion, the Sixth Circuit reasoned as follows:

> Prime contends that the second market instruction defined the tying product too narrowly as a matter of law. Prime claims that the market definition of "Ford-required CAD/CAM" must fail because this market is limited to PDGS, a single manufacturer's brand of software. *We agree.*

Pet. App. 14a (emphasis added). Undaunted by the plain language of the Sixth Circuit's opinion, Prime writes:

> The court noted cases which "reject[ed] market definitions limited to a single manufacturer's products" (*id.* at 14a-15a), *but did not rest its rejection of Virtual's claim on that ground.*

Br. in Opp. 4 (emphasis added).

Prime apparently takes the Sixth Circuit's words—"We agree"—to convey disagreement.[1] Likewise, the Sixth

[1] According to Prime, the court "*accepted Virtual's* position that '[d]efining the market by Ford's requirement[s] does *not* create a single brand market because Ford requires more than one brand.'" Br. in Opp. 4 (quoting Pet. App. 15a). The court did *quote* that argument, but it did not follow that quotation with the telltale

Circuit expressly "agree[d]" with Prime that a jury instruction "defined the tying product too narrowly as a matter of law * * * *because* this market is limited to * * * a single manufacturer's brand of software." Pet. App. 14a (emphasis added). Yet Prime claims that "[t]he opinion does *not* say that, 'as a matter of law,' a single brand can never constitute a proper market." Br. in Opp. 8. The Sixth Circuit even restated its holding in the form of a general rule: "Courts * * * consistently reject market definitions limited to a single manufacturer's products because such markets do not reflect inter-brand competition." Pet. App. 14a-15a. Remarkably, Prime contends that these crystal clear statements either do not exist or were "indisputably" dicta. Br. at Opp. 10.

As the dissent in *Kodak* observed (112 S. Ct. at 2100), *Kodak* made the Sixth Circuit's decision obsolete, along with other decisions on which the court below expressly relied in overturning the result in the district court. A relic of discredited reasoning should not continue to separate Virtual from a multimillion-dollar antitrust verdict rendered by a properly instructed jury.

1. Prime argues to this Court that "*Kodak* has no bearing on the issues decided below," and that "*Kodak* and this case * * * are different in all relevant respects." Br. in Opp. 6. Prime whistled a far different tune to the Sixth Circuit. There, Prime well perceived that this case closely parallels *Kodak* and, as noted above, submitted the government's *Kodak* amicus brief to the court of appeals. The court in turn followed much of the reasoning of the *Kodak* amicus brief—reasoning that this Court later rejected.

Prime independently duplicated the principal arguments made and rebuffed in *Kodak*. See 112 S. Ct. at 2081-2082, 2090. To combat the overwhelming evidence that its tie foreclosed hardware maintenance competition,

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words "We agree"—as it did after quoting the position that Prime espoused below but now abandons. Rather, all the court said was that it would "giv[e] Virtual every inference" but still disagreed with its position. Pet. App. 15a.

Prime argued strenuously and successfully that "[o]ne product brand does not constitute a market." Prime C.A. Br. 26. Accordingly, because "[t]he Ford-required 'market' clearly is a subset of the Prime 'brand' of CAD/CAM software," Prime C.A. Rep. Br. 10, Prime insisted that it could have no power in the aftermarket for support of Ford-required CAD/CAM software without power in the market for original sales of all CAD/CAM applications.

After *Kodak*, Prime may now regret that it so thoroughly persuaded the court of appeals. Prime may wish that the Sixth Circuit's opinion did *not* rest on the judgment that Prime could not have power in the markets for software support unless it had power in the markets for original purchases of software. But wishing does not make it so.

The Sixth Circuit refused to acknowledge the relevance of market power in aftermarkets. But cf. *Kodak*, 112 S. Ct. at 2080, 2087-2088. If the tying product market was "the sale of software revisions and support for the CAD/CAM industry in general," the court said, "the jury [had] to find that Prime possessed * * * 'market power' in the *sale of all software* suitable for CAD/CAM purposes." Pet. App. 12a (emphasis added). Virtual had argued that Prime controlled the market for "the sale of software revisions and support for software necessary to do business with Ford Motor Company" (*ibid.*), because "only Prime can market the software updates for PDGS" (*id.* at 16a). The Sixth Circuit responded:

> This argument confuses the tying product (software support for PDGS) with the interbrand market relevant for antitrust analysis [*i.e.*, "the sale of all software suitable for CAD/CAM purposes"]. This court previously has refused to ignore interbrand competition by limiting the product market to one manufacturer's product.

Ibid. That response is exactly the reasoning this Court rejected in *Kodak*.

The Sixth Circuit did not stop there. Continuing to base its analysis on grounds later rejected in *Kodak*, the court disdained the evidence of Prime's ability to raise prices in the aftermarket for PDGS software support (Pet. App. 17a), ignored the lock-in demonstrated in this case,[2] and drew inferences contrary to those this Court drew from similar facts in *Kodak*: "[W]ere Prime to charge exorbitant prices for its software support, its customers would simply switch to some other manufacturer of PDGS-type software. Prime's lack of market power over the general market for CAD/CAM software thus prevents Prime from controlling the 'submarket' for PDGS software." Pet. App. 18a. As we pointed out (Pet. 17), this Court noted that locked-in customers cannot switch so easily and "will tolerate some level of service-price increases before changing equipment brands." 112 S. Ct. at 2087. In *Kodak*, this Court held that the presence of a locked-in customer base might "foil the simple assumption that the equipment and service markets act as pure complements to one another." *Ibid.* In this case, of course, the evidence showed—and the jury presumptively found as fact—that customer lock-in *did* "foil th[at] simple assumption," but the Sixth Circuit clung to that assumption nevertheless. See Pet. 17-18.

In short, the Sixth Circuit's opinion is permeated at every important juncture with theories that this Court later rejected in *Kodak*. It is fanciful to suggest that "the result here could not be affected by reconsideration in light of *Kodak*" (Br. in Opp. 9-10). It is irresponsible for Prime to suggest that the Sixth Circuit should not even be required to take another look at this case, in light of *Kodak*, before its reversal of the damages award and a consumer-protective injunction should stand.

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[2] The Sixth Circuit discounted the evidence that users were *actually* locked in to Prime's software support on the ground that there was "a *potential* for reasonable interchangeability of supply." Pet. App. 19a (emphasis added). As we pointed out in the petition (at 18), the court of appeals read "reasonable" out of "reasonable interchangeability," forsaking "commercial realities" (112 S. Ct. at 2090) for theoretical speculation.

2. Recognizing the error in a "*Kodak*-like ruling" that market power in an aftermarket cannot exist without power in the market for original sales (Br. in Opp. 10), Prime tries to revise the record to show that no such ruling was made in this case or was pertinent to the issues presented below. Prime is entirely wrong.

The Sixth Circuit made exactly the "*Kodak*-like ruling" that Prime "cannot * * * locate[]" (Br. in Opp. 10). It wrote: "a computer manufacturer could not sustain high prices in the derivative markets for computer service and warranty protection because it lacked market power in the primary interbrand market for small business computers." Pet. App. 17a (citing *General Business Systems* v. *North American Philips Corp.*, 699 F.2d 965 (9th Cir. 1983)).[3] It then said that "[t]he same is true in this case," precisely because PDGS is Prime's brand of software and Prime "lack[s] * * * power over the general market for CAD/CAM software." Pet. App. 18a.

Prime asks this Court to blame Virtual for the Sixth Circuit's decision to restrict its analysis to the markets for "the sale of * * * software" even though the jury had evaluated markets defined in terms of "the sale of software revisions and support." Pet. App. 12a. Prime represents to this Court that "Virtual repeatedly refused to draw any distinction between an 'original market' for software and an 'aftermarket' for software support (to which hardware maintenance was tied)." Br. in Opp. 11.

Prime's representation is false. Rather than choose "to treat the software and the support package as indistinct" (Br. in Opp. 11 n.8), Virtual consistently emphasized the distinction between the two, all the way from the filing of the complaint in the district court through the rehearing petition in the court of appeals. Thus, Virtual

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[3] The Sixth Circuit's heavy reliance, in its analysis rejecting the Ford-required CAD/CAM aftermarket, on *General Business Systems* (Pet. App. 16a, 17a, 18a, 19a), underscores the dependence of the Sixth Circuit's decision on the very analysis rejected in *Kodak*. *General Business Systems* was directly superseded by *Kodak*. See 112 S. Ct. at 2100 (Scalia, J., dissenting).

alleged at the outset "[t]hat Defendant has sufficient economic power within the *Ford CAD/CAM market* as well as other CAD/CAM markets *with respect to software updates, revisions and improvements* so as to restrain a not insubstantial amount of commerce." C.A. App. 31-32 (Second Amended Complaint ¶ 23) (emphasis added). Virtual explained to the Sixth Circuit that "Software Support is a separate and distinct product which a customer can purchase after buying the original software" (Virtual C.A. Br. 6) and added that at issue in this case was "Prime's tie of hardware maintenance to *Software Support*" (*id.* at 7 (emphasis added)). See generally *id.* at 7-10 (explaining distinction between software and software support); C.A. App. 1472-1473 (trial testimony making same point).[4] Finally, Virtual reminded the court that it had "ignore[d] market power over software support." Virtual Pet. Reh. 7 (citing Ninth Circuit decision in *Kodak*). Like both courts below, Virtual occasionally used shorthand to describe the markets at issue, but never did it retreat from the position that this case concerns software support as opposed to initial software sales. Prime's assertion to the contrary (Br. in Opp. 11) relies on quotations of such shorthand without any surrounding context.

3. Prime makes the astonishing assertion that Virtual "really does not dispute" three "basic rulings" by the Sixth Circuit. Br. in Opp. 6. The petition in fact shows that each of the rulings that Prime recites cannot stand after *Kodak*.

First, notwithstanding Prime's assertion that in this Court Virtual has "all but abandoned" the argument "that Prime had market power in 'the market for revisions and support for the CAD/CAM industry in general'" (Br. in Opp. 3), the petition thoroughly demon-

[4] Virtual further explained that "[t]he markets for hardware sales and software sales are not at issue in this case" (Virtual C.A. Br. 5), and cautioned, "Although *Prime* continues to discuss competition in these markets, that competition is irrelevant" (*id.* at 5 n.4 (emphasis added)).

strates the Sixth Circuit's error in rejecting that argument. Pet. 22-25. The Sixth Circuit did not merely hold "that Prime's possession of 11% of the worldwide market for CAD/CAM support services * * * does not establish the requisite market power for a *per se* violation." Br. in Opp. 6. Rather, as we pointed out (Pet. 22), the court rested entirely on the "formalistic distinction[]" provided by the isolated statistic of market share, at the expense of analysis of "forcing" and "actual market realities" as this Court required in *Kodak*, 112 S. Ct. at 2080 & n.9, 2082.[5] "When such 'forcing' is present, competition on the merits in the market for the tied item is restrained and the Sherman Act is violated." *Id.* at 2080 n.9 (quoting *Jefferson Parish*, 466 U.S. at 12).

Second, we refuted the Sixth Circuit's strained "single customer" analysis on its own terms, showing why the Ford-required CAD/CAM aftermarket, containing hundreds of suppliers, is no different in economic terms from any other market in which customers are locked into a single brand. Pet. 19-20.[6] We also noted what Prime

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[5] *Kodak* thoroughly undermines all aspects of the Sixth Circuit's opinion. Prime claims that in truncating its market analysis after considering the 11% figure, without considering the structure of the particular market, the Sixth Circuit "routine[ly] appli[ed] *Jefferson Parish* [*Hosp. Dist. No. 2* v. *Hyde*, 466 U.S. 2 (1984),]" and that "decisions of this Court and those of other circuits * * * strongly confirm" that course. Br. in Opp. 13. Prime cites only the Sixth Circuit opinion (Pet. App. 12a), which in turn cites from this Court only *Jefferson Parish* (the misapplication of which we exposed, Pet. 22-25), and from the circuits two more cases that the *Kodak* dissent observed could no longer stand in light of *Kodak*. See 112 S. Ct. at 2100 (citing *Grappone, Inc.* v. *Subaru of New England, Inc.*, 858 F.2d 792 (1st Cir. 1988), and *A.I. Root Co.* v. *Computer/Dynamics, Inc.*, 806 F.2d 673 (6th Cir. 1986)).

[6] Prime's assertion that "Ford was capable of compelling Prime to change its PDGS pricing, and had done so," Br. in Opp. 14 n.9, crumbles on perusal of the record. The *software* price was "reduced only to reflect the royalty reduction" (C.A. App. 817), that is, the only change in *software* pricing reflected "Ford's reduced software royalty" (*id.* at 816). The agreement allowed Prime to *increase* its revenues from software maintenance substantially (*id.* at 823, 826-

would have this Court overlook: the Sixth Circuit's foray into "single customer" theory followed, and flowed from, its flat and dispositive refusal to recognize a single-brand aftermarket. Pet. 15-16. The Sixth Circuit labeled its discussion of the "single customer" issue as a response to Virtual's "attempt[] to avoid * * * authority" that rejected single-brand aftermarkets (Pet. App. 15a), authority that *Kodak* stripped of precedential value.

Finally, we countered the Sixth's Circuit's dictum implying "that market foreclosure of 2% of a proposed single brand market * * * does not constitute a rule-of-reason violation." Br. in Opp. 6. To begin with, we pointed out, the Sixth Circuit explicitly rested its denial of the rule-of-reason claim on the same aversion to single-brand markets that led it erroneously to reject the Ford-required CAD/CAM aftermarket—an aversion that *Kodak* should cure. Pet. 20-22.

In addition, we emphasized that, by foreclosing $12 million in profits in Virtual's territory alone, Prime's tie had a substantial "actual adverse effect on competition" under the rule of reason. Pet. 21-22 (quoting *Jefferson Parish*, 466 U.S. at 31).[7] No rule of antitrust law allows a defendant to gouge an identifiable group of consumers of millions of dollars by anticompetitive means so long as those consumers constitute only a small fraction of some "market," but that is the logical conclusion of Prime's effort to ascribe significance to the utterly irrelevant "2%" figure. If it is " 'unreasonable, *per se*, to foreclose competitors from any substantial market' by a tying arrangement," *Fortner Enterprises, Inc.* v. *United States Steel Corp.*, 394 U.S. 495, 501 (1969) (quoting

827), and to preserve its huge profit margin on original sales of PDGS (*id.* at 1494-1495, 1562).

[7] See also *United States* v. *Loew's Inc.*, 371 U.S. 38, 49 (1962) (tying arrangements foreclosing as little as $60,800 of business restrained trade "both by their 'inherent nature' and by their 'effect' "); *id.* at 48 ("no question * * * [that] adverse effects on free competition" resulted from contracts between independent film distributors and individual television stations).

International Salt Co. v. *United States*, 332 U.S. 392, 396 (1947)), it can hardly be legitimate under the rule of reason forcibly to withdraw a competitive choice from a substantial number of consumers, simply because other consumers may retain the choice.

In this case, the 2% figure is especially misleading because it reflects the number of Prime 50 Series computer users who are also PDGS users, *not* the number of computer users who are victims of Prime's anticompetitive tying arrangements. Prime maintains a 97% market share in hardware maintenance of its 50 Series computers (C.A. App. 722), and uses its tying program—which covers almost all of the software that it distributes (C.A. App. 1653; Pet. 7)—as protection from competitive pressures (C.A. App. 723; see also C.A. App. 1416-1418). Because Virtual's detailed proof was limited to the customers for whom it sought to compete with Prime, Prime claims that the tie must be reasonable under the antitrust laws, but that simply does not follow.

4. It is not difficult to discern the reason for Prime's desperate plea that *Kodak* bears no relation to this case, despite Prime's successful argument to the Sixth Circuit that exactly the reasoning that this Court rejected in *Kodak* should control that court's decision. Prime was caught red-handed when it used its tying policy to force computer owners to forgo Virtual's less expensive service. Those customers' protests reached the jury, and the jury saw Prime's tactic for what it was—a clear violation of the antitrust laws.

Prime successfully induced the Sixth Circuit to overturn the jury's verdict by relying on abstract theories that this Court later rejected in *Kodak*. Prime (and with it the Sixth Circuit) read earlier cases of this Court in ways that are no longer tenable after *Kodak* and relied on several circuit court cases that, as the *Kodak* dissent noted, *Kodak* wiped off the slate. After Prime thought it had dodged a bullet, *Kodak* trained antitrust scrutiny directly onto schemes like the tie in this case.

We believe that *Kodak* ultimately compels reversal of the judgment of the court of appeals and (along with *Griffin* v. *United States*, 112 S. Ct. 466 (1991)) compels affirmance of the judgment of the district court. Without doubt, the postulates rejected in *Kodak* so pervade the decision of the Sixth Circuit that certiorari should be granted, the judgment vacated, and the case remanded for consideration in light of intervening Supreme Court precedent.

For the foregoing reasons and those given in the petition, the petition for a writ of certiorari should be granted, the judgment below should be vacated, and the case should be remanded for further consideration in light of *Kodak* and *Griffin*. In the alternative, the petition for a writ of certiorari should be granted, and the case should be set for full briefing and argument.

Respectfully submitted.

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